

## Message Text

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ACTION EUR-25

INFO OCT-01 EA-11 ISO-00 CIAE-00 DODE-00 PM-07 H-03 INR-10

L-03 NSAE-00 NSC-10 PA-03 RSC-01 PRS-01 SS-15 USIA-15

AID-20 EB-11 FRB-02 XMB-07 OPIC-12 CIEP-02 LAB-06

SIL-01 OMB-01 STR-08 CEA-02 DRC-01 /178 W

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R 072105Z SEP 73

FM AMEMBASSY LONDON

TO SECSTATE WASHDC 3872

INFO AMEMBASSY BERN

AMEMBASSY BONN

AMEMBASSY BRUSSELS

AMEMBASSY COPENHAGEN

AMEMBASSY DUBLIN

AMEMBASSY LUXEMBOURG

AMEMBASSY PARIS

AMEMBASSY ROME

AMEMBASSY STOCKHOLM

AMEMBASSY THE HAGUE

AMEMBASSY TOKYO

USMISSION EC BRUSSELS

USMISSION OECD PARIS

USDOC WASHDC

TREASURY DEPT WASHDC

UNCLAS SECTION 01 OF 03 LONDON 10330

DEPARTMENT FOR FRB

E.O. 11652:N/A

TAGS. ECON, UK

SUBJECT: ECONOMIC DEVELOPMENTS - WEEK ENDING SEPTEMBER 7

BEGIN SUMMARY: THIS WEEK THE POUND MOVED STEADILY DOWN-  
WARD AGAINST THE DOLLAR, BUT TOOK A SHARP DIVE ON

WEDNESDAY AND THURSDAY MORNING UNTIL BANK OF ENGLAND

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INTERVENTION AND AN ANNOUNCEMENT BY THE TREASURY OF THE

EXTENSION OF THE STERLING AGREEMENTS FOR SIX MONTHS REVERSED THIS DRAMATIC FALL. STERLING FELL AS LOW AS \$2.3780, BUT RECOVERED TO CLOSE AT \$2.4240 FOR THE DAY. STERLING'S DEPRECIATION AGAINST THE WEIGHTED AVERAGE OF ALL CURRENCIES REACHED 20.35 PERCENT AT ONE POINT ON THURSDAY, BUT RECOVERED TO 18.63 PERCENT AT THE CLOSE. GOLD TRADED BETWEEN \$103.50 AND \$105.50 AN OUNCE THIS WEEK AND CLOSED ON THURSDAY AT \$105.50. UK OFFICIAL RESERVES FELL BY \$112 MILLION DURING AUGUST TO STAND AT \$6,516 MILLION AT THE END OF THE MONTH. UK BALANCE OF PAYMENTS FOR THE SECOND QUARTER SHOWED A TOTAL NET CURRENCY INFLOW OF 377 MILLION POUNDS. OUTFLOWS ARISING FROM THE CURRENT ACCOUNT DEFICIT OF 166 MILLION POUNDS (N.S.A.) AND CAPITAL TRANSFERS OF 19 MILLION POUNDS WERE MORE THAN OFFSET BY A NET INFLOW OF 559 MILLION POUNDS FROM IDENTIFIED INVESTMENT AND OTHER CAPITAL TRANSACTIONS, INCLUDING ALMOST 290 MILLION POUNDS IN PUBLIC SECTOR BORROWING. THE PRIME MINISTER AND THE CHANCELLOR, THIS WEEK, BOTH REITERATED THE GOVERNMENT'S COMMITMENT TO GROWTH AS ITS ECONOMIC OBJECTIVE. WHILE CAPITAL EXPENDITURE BY UK MANUFACTURING INDUSTRY ROSE BY 7 PERCENT BETWEEN SECOND HALF 1972 AND FIRST HALF 1973, THE LATEST FT SURVEY OF BUSINESS OPINION SEES SHORTAGES OF LABOR AND RAW MATERIALS AS INCREASINGLY INHIBITING PRODUCTION IN THE UK. LATEST FIGURES ON RETAIL SALES INDICATE CONSUMER SPENDING IS UP AGAIN FOLLOWING THE POST-VAT DOWNTURN. HIRE PURCHASE AND OTHER INSTALLMENT CREDIT BUSINESS FELL BY 7 PERCENT WHEN THE PERIOD OF FEBRUARY-APRIL IS COMPARED TO MAY-JULY. MONEY WAS EXTREMELY TIGHT IN THE PERIOD FROM MID-JULY TO MID-AUGUST, AND LLOYDS WAS UNABLE TO MEET THE OFFICIALLY REQUIRED RESERVE RATIO. IMPORT PRICES HAVE RISEN 32 PERCENT IN THE LAST 12 MONTHS. THE FINANCE HOUSES ASSOCIATION ANNOUNCED ON AUGUST 31 AN INCREASE FROM 9 PERCENT TO 12 PERCENT IN THEIR LENDING RATE. END SUMMARY

1. STERLING CLOSED AT \$2.4564-1/2 ON MONDAY (SEPTEMBER 3). ON WEDNESDAY, AFTER HECTIC TRADING AND BANK OF ENGLAND INTERVENTION, THE POUND CLOSED AT \$2.4230. IN THE FIRST TWO HOURS OF TRADING ON THURSDAY, THE POUND UNCLASSIFIED

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DROPPED MORE THAN 4 CENTS AGAINST THE DOLLAR AND WAS QUOTED AT ONE POINT AT \$2.3780. THE FALL WAS ARRESTED BY SUBSTANTIAL AND DETERMINED OFFICIAL SUPPORT BY THE BANK OF ENGLAND (ESTIMATED AT \$100 MILLION) AROUND LUNCH TIME. THE RECOVERY WAS SUSTAINED IN THE AFTERNOON BY THE ANNOUNCEMENT OF A BRITISH DECISION TO EXTEND THE STERLING AGREEMENTS FOR A FURTHER SIX MONTHS FROM THEIR EXPIRATION ON SEPTEMBER 24 (DETAILS FOLLOW BY AIRGRAM). THE POUND

CLOSED AT \$2.4240, ABOUT THE SAME LEVEL AS WEDNESDAY'S CLOSE. AT ONE POINT ON THURSDAY THE TRADE-WEIGHTED DEVALUATION WAS 20.35 PERCENT, BUT IT ENDED THE DAY AT 18.63 PERCENT. REASONS FOR THE FALL IN THE POUND INCLUDE SELLING BY THE GERMAN BANKS, BAD UK RESERVE FIGURES, EXPECTATION OF BAD TRADE FIGURES NEXT WEEK, AS WELL AS NO SIGNS YET THAT THE GOVERNMENT WILL ACT TO SLOW GROWTH IN THE ECONOMY WHICH SOME OBSERVERS BELIEVE NECESSARY. GOLD REMAINED RELATIVELY QUIET THIS WEEK WITH A LOW OF \$103.50 (LAST FRIDAY, AUGUST 31) AND A HIGH OF \$106.25 ON WEDNESDAY (SEPTEMBER 5).

2. UK OFFICIAL RESERVES FELL BY \$112 MILLION DURING

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L-03 NSAE-00 NSC-10 PA-03 RSC-01 PRS-01 SS-15 USIA-15

AID-20 EB-11 FRB-02 XMB-07 OPIC-12 CIEP-02 LAB-06

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R 072105Z SEP 73

FM AMEMBASSY LONDON

TO SECSTATE WASHDC 3873

INFO AMEMBASSY BERN

AMEMBASSY BONN

AMEMBASSY BRUSSELS

AMEMBASSY COPENHAGEN

AMEMBASSY DUBLIN

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AUGUST TO STAND AT \$6,516 MILLION AT THE END OF THE MONTH. THIS WAS AFTER RECEIPTS OF \$290 MILLION FROM PUBLIC SECTOR FOREIGN CURRENCY BORROWING AND A LONG TERM DEBT SERVICING PAYMENT OF \$14 MILLION ON A PORTUGUESE STERLING BOND. THUS, THE TOTAL COST TO RESERVES IN AUGUST WAS \$388 MILLION. SINCE THE SPECIAL PROGRAM OF PUBLIC SECTOR BORROWING ABROAD TO EASE BRITAIN'S PROBLEMS BEGAN IN MARCH, A TOTAL OF \$1,437 MILLION HAS BEEN BORROWED. THE FIGURES OF \$112 MILLION AND \$6,516 MILLION UNCLASSIFIED

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ARE RESPECTIVELY EQUIVALENT TO 38 MILLION POUNDS AND 2,251 MILLION POUNDS IF CONVERTED AT THE PARITY RATE OF ONE POUND EQUALS \$2.89524 OR 46 MILLION POUNDS AND 2,650 MILLION POUNDS IF CONVERTED AT THE CLOSING MARKET RATE ON AUGUST 31 OF ONE POUND EQUALS \$2.4585.

3. SECOND QUARTER UK BALANCE OF PAYMENTS SHOW A CURRENT ACCOUNT DEFICIT OF 198 MILLION POUNDS (S.A.) WITH A DEFICIT OF 396 MILLION POUNDS ON VISIBLE TRADE AND A SURPLUS OF 198 MILLION POUNDS ON INVISIBLES. THE TOTAL CURRENCY FLOW WAS 377 MILLION POUNDS WHICH WAS ADDED TO RESERVES. DETAILS FOLLOW BY AIRGRAM.

4. THE PRIME MINISTER, MR. HEATH, REAFFIRMED HIS "GO FOR GROWTH" PLEDGE IN A SPEECH THIS WEEK. THE CHANCELLOR, MR. BARBER, ALSO STRESSED AGAIN THE GOVERNMENT'S ECONOMIC STRATEGY YESTERDAY (SEPTEMBER 6). HE EXPLAINED THE "GO FOR GROWTH" PLEDGE IN THE CONTEXT OF THE BUDGET STRATEGY, EMPHASIZING THAT THE 5 PERCENT GROWTH PER YEAR TARGET FOR THE PERIOD SECOND HALF 1972 TO FIRST HALF 1974 WAS AN AVERAGE RATE. IN FACT, HE SAID THE RATE HAS BEEN FASTER AT THE START AND IS SLOWER NOW. HE ADDED THAT, TO AVOID A RETURN TO STOP GO, "THE RATE OF GROWTH OF DEMAND MUST NOT EXCEED THE GROWTH OF THE NATION'S PRODUCTIVE POTENTIAL, ONCE THE (UK HAS) REACHED THE LIMITS OF CAPACITY." FINALLY, HE STRESSED AGAIN THAT HE WAS READY TO ACT ON DEMAND AT ANY TIME OF THE YEAR, IN EITHER DIRECTION, IF THE SITUATION SHOULD WARRANT IT. ON PRESENT FORM HE SAW NO NEED FOR FURTHER ACTION.

5. CAPITAL EXPENDITURE BY UK MANUFACTURING INDUSTRY WENT UP BY 7 PERCENT BETWEEN SECOND HALF 1972 AND FIRST HALF 1973. THIS IS THE FIRST UPTURN SINCE THE CYCLICAL

DECLINE IN MANUFACTURING INVESTMENT WHICH STARTED EARLY IN 1971; AND IS A HIGHER RATE OF INCREASE YEAR ON YEAR THAN THE 5 PERCENT RISE INDICATED BY THE LAST DTI SURVEY. MANUFACTURING INVESTMENT FELL SLIGHTLY FROM 463 MILLION POUNDS IN FIRST QUARTER 1973 TO 460 MILLION POUNDS SECOND QUARTER 1973. THE REVIVAL IN MANUFACTURING INDUSTRY'S STOCK BUILDING HAS CONTINUED WITH STOCKS NOW STANDING AT THE END OF JUNE AT 9,513 MILLION POUNDS.  
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6. THE LATEST FINANCIAL TIMES SURVEY OF BUSINESS OPINION SUGGESTS THAT THE SYMPTOMS OF OVERHEATING IN THE ECONOMY HAVE BECOME MORE AND MORE APPARENT IN RECENT WEEKS. THE SURVEY SHOWS THAT PRODUCTION AND ORDERS HAVE CONTINUED TO EXPAND FAST IN THE LAST FEW MONTHS, AND THAT INDUSTRIALISTS STILL EXPECT BUOYANT CONDITIONS OVER THE NEXT YEAR. THE GENERAL LEVEL OF BUSINESS CONFIDENCE HOWEVER HAS DECLINED SOMEWHAT, AND THIS MAY BE ASSOCIATED WITH A SHARP INCREASE IN THE NUMBER OF COMPANIES CONCERNED ABOUT THE SUPPLY OF SKILLED AND UN-SKILLED LABOR, AND RAW MATERIALS.

7. THE VOLUME OF RETAIL SALES ROSE IN JULY TO 115.9 (1966100), A RISE OF 1 PERCENT ON JUNE. THE INDEX HAD DROPPED SHARPLY IN APRIL AND MAY. SALES HAVE BEEN RECOVERING SINCE MAY, AND THE JULY OUT-TURN CONFLICTS WITH THE TREASURY'S TENTATIVE SUGGESTION IN ITS AUGUST ECONOMIC REVIEW THAT "RETAIL SALES IN JULY MAY SHOW LITTLE CHANGE FROM THEIR JUNE LEVEL." RETAIL SALES ACCOUNT FOR ABOUT HALF OF TOTAL CONSUMER SPENDING.

8. HIRE PURCHASE AND OTHER INSTALLMENT CREDIT BUSINESS ADVANCED IN JULY TO 235 MILLION POUNDS OF NEW INSTALLMENT CREDIT (S.A.) FROM 225 MILLION POUNDS IN JUNE. TOTAL DEBT OUTSTANDING IS NOW 2,284 MILLION POUNDS. THE CONTRIBUTION OF HIRE PURCHASE CREDIT TO CONSUMER SPENDING HAS BEEN MUCH SMALLER IN RECENT MONTHS THAN DURING THE FIRST QUARTER.

9. THE RESERVE RATIOS OF THE CLEARING BANKS FELL IN THE PERIOD OF MID-JULY TO MID-AUGUST. AN EXPANSION IN

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ACTION EUR-25

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L-03 NSAE-00 NSC-10 PA-03 RSC-01 PRS-01 SS-15 USIA-15

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R 072105Z SEP 73

FM AMEMBASSY LONDON

TO SECSTATE WASHDC 3874

INFO AMEMBASSY BERN

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ARBITRAGE OPERATIONS BY CORPORATE BORROWERS LAST MONTH  
RESULTED IN AN EXCEPTIONAL RISE OF NEARLY 600 MILLION  
POUNDS IN THE LONDON CLEARING BANKS' STERLING ADVANCES.  
WITH ALMOST 200 MILLION POUNDS BEING SIPHONED OFF TO MEET  
THE BANK OF ENGLAND'S CALL FOR SPECIAL DEPOSITS, THE  
BANKS' LIQUIDITY POSITIONS DETERIORATED SHARPLY. LLOYDS  
RESERVE RATIO OF LESS THAN 12.5 PERCENT WAS LOOKED UPON  
SERIOUSLY BY THE BANK OF ENGLAND. THE BANKS ARE FACING A  
SERIOUS LIQUIDITY PROBLEM EVEN WITH BASE RATES AT 11  
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PERCENT. THIS SITUATION HAS INTENSIFIED SPECULATION THAT A CHANGE IN OFFICIAL CREDIT CONTROLS IS NOT FAR AWAY.

10. THERE WAS A FURTHER INCREASE IN IMPORT PRICES OF NEARLY 3 PERCENT IN JULY WHICH BROUGHT THE INCREASE OVER THE PAST YEAR TO 32 PERCENT. THE JULY RISE LED TO A FURTHER DETERIORATION IN THE UK TERMS OF TRADE WHICH HAS NOW FALLEN ON AN INDEX BASIS FROM 111 IN JULY 1972 TO 94 (1961=100). EXPORT PRICES ROSE BY 1-1/2 PERCENT IN JULY TO STAND AT 11-1/2 PERCENT ABOVE A YEAR AGO.

11. THE FINANCE HOUSES ASSOCIATION HAS RAISED ITS LENDING RATE FROM 9 PERCENT TO 12 PERCENT. THIS FOLLOWS THE MOVE BY THE CLEARING BANKS TO RAISE THEIR BASE LENDING RATE TO 11 PERCENT, AND REFLECTS THE UPWARD TREND OF 3 MONTHS' INTER-BANK INTEREST RATES.

12. THE FORWARD DISCOUNT ON STERLING NARROWED AT THE BEGINNING OF THE WEEK BUT WIDENED VERY MARKEDLY ON WEDNESDAY (SEPTEMBER 5) IN RESPONSE TO THE SLIDE IN STERLING-DOLLAR RATE. ON THURSDAY (SEPTEMBER 6) THE DISCOUNT NARROWED AGAIN.

|          | 8/30 | 9/6  | CHANGE  |
|----------|------|------|---------|
| 1 MONTH  | 0.98 | 1.15 | UP 0.17 |
| 3 MONTHS | 2.78 | 2.85 | UP 0.07 |
| 6 MONTHS | 4.75 | 5.00 | UP 0.25 |

(ALL FIGURES IN CENTS)

13. LOCAL AUTHORITY DEPOSIT RATES DRIFTED DOWNWARD DURING THE WEEK UNTIL THURSDAY (SEPTEMBER 6) WHEN THEY ROSE marginally.

|          | 8/30   | 9/6      | CHANGE    |
|----------|--------|----------|-----------|
| 1 MONTH  | 13-7/8 | 13-1/4   | DOWN 5/8  |
| 3 MONTHS | 14     | 13-7/8   | DOWN 1/8  |
| 6 MONTHS | 14     | 13-11/16 | DOWN 5/16 |

14. EURO-DOLLAR RATES FLUCTUATED WITHIN A VERY SMALL RANGE THIS WEEK.

|         | 8/30   | 9/6    | CHANGE    |
|---------|--------|--------|-----------|
| 1 MONTH | 11-1/2 | 11-1/2 | UNCHANGED |

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|          |        |        |          |
|----------|--------|--------|----------|
| 3 MONTHS | 11-5/8 | 11-1/2 | DOWN 1/8 |
| 6 MONTHS | 11-5/8 | 11-1/2 | DOWN 1/8 |

15. GOLD CLOSED AT \$105.50 ON THURSDAY, UP \$5.00 FROM LAST THURSDAY'S CLOSE.

16. THE MINIMUM LENDING RATE REMAINED AT 11-1/2 ON

FRIDAY, SEPTEMBER 7.

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## Message Attributes

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**TAGS:** ECON, UK  
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**Type:** TE  
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